

# Online Research @ Cardiff

This is an Open Access document downloaded from ORCA, Cardiff University's institutional repository: <https://orca.cardiff.ac.uk/id/eprint/123073/>

This is the author's version of a work that was submitted to / accepted for publication.

Citation for final published version:

Editorial Team, WER 2000. Economic commentary. Welsh Economic Review 12 (2) , pp. 20-22. 10.18573/wer.151 file

Publishers page: <http://dx.doi.org/10.18573/wer.151>  
<<http://dx.doi.org/10.18573/wer.151>>

Please note:

Changes made as a result of publishing processes such as copy-editing, formatting and page numbers may not be reflected in this version. For the definitive version of this publication, please refer to the published source. You are advised to consult the publisher's version if you wish to cite this paper.

This version is being made available in accordance with publisher policies.

See

<http://orca.cf.ac.uk/policies.html> for usage policies. Copyright and moral rights for publications made available in ORCA are retained by the copyright holders.







**CARDIFF**  
.....  
**BUSINESS**  
.....  
**SCHOOL**

# Welsh Economic Review

Volume 12.2 Autumn 2000

Produced in association with



# Welsh Economic Review



**Review**



# Economic Commentary

## The World Economy

The world economy is expected to have grown by over 3% during 2000 (OECD). Figure 1 below, shows real GDP growth in 1999 and OECD forecasts for a number of countries in 2000 and 2001. This is the first time since 1994 that growth is expected to increase in all major countries. The National Institute of Economic and Social Research (NIESR) estimated growth in the Euro zone to be 3.2% (annualised) to the first quarter of 2000 and predicted it to peak at 3.4% in 2000, with the main contributing factor being an improved balance of trade. NIESR estimates tend to be slightly more optimistic than the OECD measures shown in Figure 1. NIESR forecast a GDP growth rate of around 5% in 2000 and 5.75% in 2001 in the Asian economies, buoyed by strong demand for electronics and IT products, despite continued weakness in Japan.

In the 12 months to March 2000 economic growth in Japan was at 0.5%, well below the government's target. Business confidence in the Japanese economy is declining. For example, there has been a sharp increase in the number of bankruptcies, which by May 2000 were up by 13% on the previous years total. In October 1998 a government scheme was implemented offering emergency loan guarantees. More than 1.3m businesses have used the funding, but a number of firms are now folding under the added financial pressure, and in 2001 some 65,000 companies are expected to default.

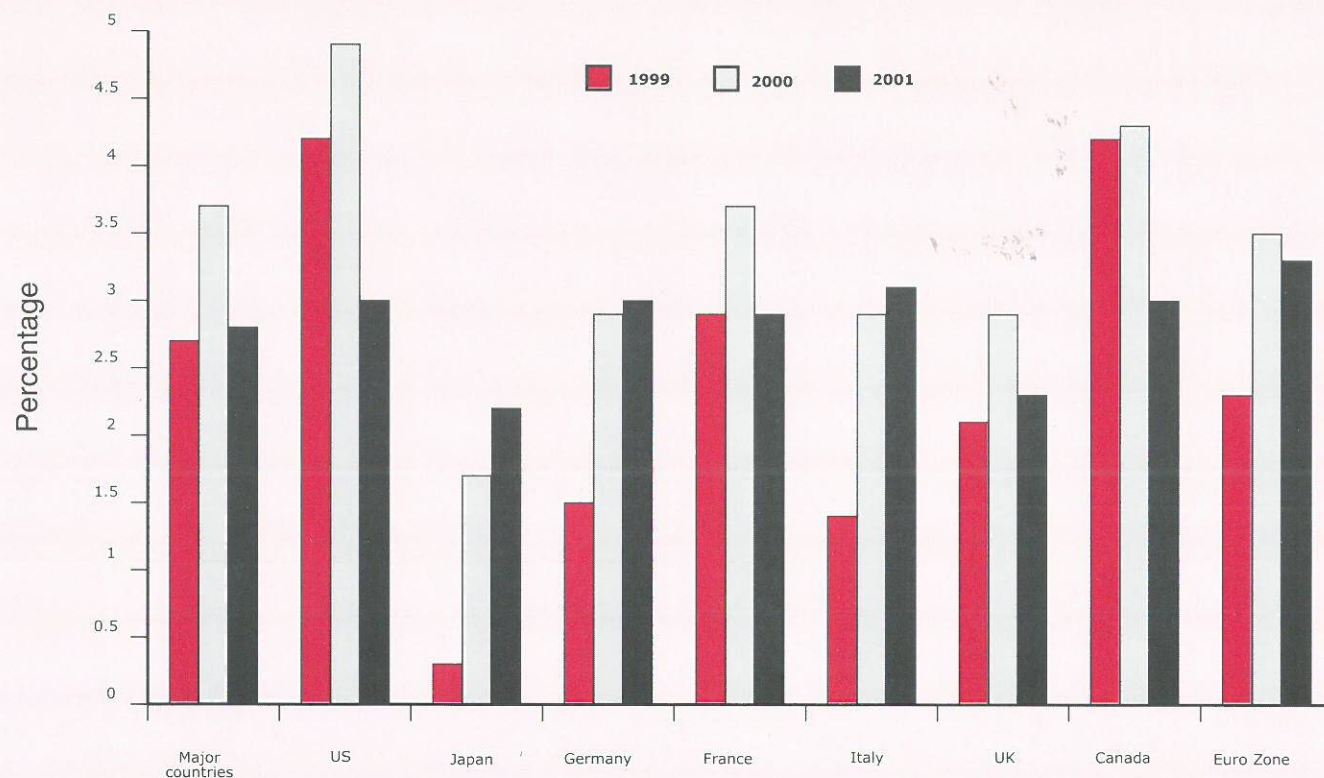
Productivity growth in the Euro zone (Euro-11) was 0.6% for 1999, the lowest on record since 1975. In recent decades the Euro zone has outpaced America for productivity growth. For example from 1973 to 1995 productivity growth averaged 1.6%-1.7% in France and Germany compared to just 0.4% in

America. However, America overtook the Euro zone in 1995 and has experienced substantial productivity growth since, whilst in the Euro zone productivity growth has been poor over the past two years.

The recent downturn in productivity growth in the Euro zone has been partly the result of a cyclical economic slowdown, accompanied by a reluctance for firms to lay-off workers because of rigid employment protection laws. In addition, there have been reductions in the rate of technological progress. Slower productivity growth may also simply be an effect of labour market reforms in Netherlands, France and Spain, for example, which have encouraged firms to employ more young, part-time or unskilled workers. This may have increased the need for firms to use more resources to achieve greater output, resulting in lower productivity. Euro countries which have

**Figure 1 Real GDP Growth in 1999 and OECD Projected Growth in 2000 and 2001**

The figure below shows real GDP growth in 1999 and OECD forecasts for real GDP growth in 2000 and 2001. The OECD expects GDP growth in the world's major economies to peak in 2000 at 3.7% before falling to 2.8% by 2001. The Euro-zone is projected to continue growing at 3.3% per annum into 2001, two of the main contributors being Germany and Italy both of which are currently experiencing strong growth. Although the US and Canada have real GDP growth in 1999 and 2000 higher than the average for major economies, their 2001 growth is expected to decline sharply, and is forecast to be outpaced by growth in the Euro zone.



Source: OECD Economic Outlook June 2000



done little to deregulate labour markets, such as Germany and Italy, have achieved greater productivity growth (The Economist, April 15<sup>th</sup>-21<sup>st</sup> 2000, p105).

Inflation in the US remains relatively subdued. Retail sales grew by 0.5% in June 2000, the largest monthly gain since February, although the majority of this rise was due to greater car sales. Factory output over the period April-June 2000 grew at 7%, the fastest acceleration in four years (US Federal Reserve). Surging energy prices, in particular oil, raise concerns about the potential for wage and price increases throughout the US economy.

### The UK Economy

The latest figures from the National Institute of Economic and Social Research (NIESR) estimated that the UK economy grew at 0.8% in the three months to June 2000. The service sector grew by 0.8% in the second quarter, whilst manufacturing growth fell by 0.5% (PriceWaterhouseCoopers), not helped by the adverse effects of a strong pound weakening the competitiveness of UK exports. Indeed, whilst the general consensus among forecasters is that the economy will expand strongly in 2000 (by around 2.8%), manufacturing will probably remain subdued, with growth at around 1% (NIESR). The difficulties experienced by the manufacturing sector were highlighted by the CBI Industrial Trends Survey, an index of business optimism, which fell from a peak of +13 in October 1999 to +9 in January 2000 and then declined further to -2 in April 2000. Despite the effects of a strong pound, the trade deficit declined during the first quarter of 2000 from £1.4bn to £1.1bn.

In October the Monetary Policy Committee again decided to keep interest rates at 6%, unchanged since the start of the year, despite average earnings well above the 4.5% reference value that the MPC sees as consistent with its 2.5% inflation target. Interest rates remain unchanged despite evidence of growing consumer expenditure, with consumer credit increasing by £1.6bn in May, the biggest monthly rise since records began in 1993 (Primark Datastream). Growing confidence amongst consumers is also reflected in a falling savings ratio - the proportion of disposable income not spent - which, during the first quarter stood at 3.8%, down from 5% in the fourth quarter of 1999 (Primark Datastream). During the first quarter of 2000 GDP grew at a rate below its long run trend, suggesting that demand is growing less quickly than supply, so

easing inflationary tendencies. Furthermore, a strong pound has led to deflationary pressure, and the underlying inflation rate excluding mortgage interest payments, undershot the MPC target of 2.5% for the whole of 1999.

Discussions concerning the potentially damaging repercussions upon foreign direct investment (FDI) of remaining outside the Euro zone continue. However, in the year to March 2000 foreign inward investment into Britain rose by 23%, and a survey of foreign banks by the Chamber of Commerce and Industry (CCI) found that participation in the Euro by Britain was ranked 21<sup>st</sup> out of 23 factors influencing location.

Not surprisingly, given the pressures upon manufacturing, the majority of employment growth in 2000 has been in the service sector, and largely accounted for by part-time jobs (in contrast to the fourth quarter of 1999, where full-time jobs showed the largest increase, PriceWaterhouseCoopers). Between February and April 2000 the total ILO rate of unemployed fell by 0.2 percentage points. However, there remain clear differences in unemployment trends across the UK regions. The ILO rate fell most in the East Midlands (by -0.7 percentage points) but increased in Scotland by 0.4 percentage points (ONS).

### The Welsh Economy

Average earnings increased by 5.8% in the year to March 2000 (Office for National Statistics), although growth was faster in the private sector (6.2%, compared to 4.2% in the public sector). The unemployment rate during the period February to April 2000 for those individuals aged 16+ averaged 6.5% (ILO measure), a change on 1999 of -0.9 percentage points. This is the lowest rate for some 20 years but was above the UK average of 5.7% for the same period. Wales continues to suffer from job losses in the manufacturing sector, where between December 1998 and December 1999, employment fell by 2.8%. Other sectors experienced employment growth over the same period (ONS).

The continuing strength of Sterling has detrimentally affected the Welsh manufacturing sector, impacting upon business confidence in Wales. A survey by the Confederation of British Industry and Business Strategies found that overall business confidence and export optimism in Wales declined during the second quarter of 2000. Whilst manufacturing job losses, as a result of a strong currency, are not just a Welsh

phenomenon, over a fifth of total Welsh employment is in manufacturing compared to a much smaller share for the UK as a whole.

There are further concerns that Welsh indigenous business is weak in terms of its competitiveness, ranked 11<sup>th</sup> out of 12 UK regions (Huggins, 2000). Moreover, business start-up rates (per head of the population) in Wales are also much lower than other UK regions (DTI 2000) whilst the growing competitiveness of Central and Eastern European economies - particularly Poland, the Czech Republic and Hungary - has impacted upon Welsh manufacturing.

Despite worries over manufacturing, there has been some good news with a number of important employment announcements in a variety of sectors (see Diary Section).

### Regional GDP Estimates

Provisional regional GDP estimates for 1998 have recently been published by the Office for National Statistics (ONS). The methodology used to estimate GDP at a national and regional level has been changed, largely as a result of the on-going implementation of the European System of Accounts (ESA95). Regional GDP estimates since 1989 have now been adjusted to reflect these changes and hence to provide a consistent time-series. The 1998 estimates and further information about the changes are published by the ONS in the August 2000 issue of *Economic Trends* pp87-103.

The ONS (provisionally) estimate 1998 Welsh GDP at £29bn, which was 3.9% of UK GDP, whilst Welsh GDP per head (£9,900) was estimated to be 79.4% of UK levels, compared with 83.2% in 1990 (calculated on the same basis). In 1998 Welsh GDP per capita levels were just above those of the North East of England (78.8%) and Northern Ireland (75.8%), but below all other regions of the UK.

Figures 2 and 3 over page show a time series of Welsh GDP per capita, and regional GDP per capita in 1998.

### Forecasts

In the last issue of the *Welsh Economic Review*, WERU forecast change in real GDP for Wales of 0.4% for 1999, 2% for 2000, and 2.1% for 2001 and 2002.

Whilst regional GDP estimates for 1999 are not expected to be published by ONS until Spring 2001, real GDP may have grown more than expected during 1999. Despite continuing manufacturing



job losses during 1999, manufacturing sector output actually increased. Moreover during 1999 service sector employment increased. Largely as a result of a stronger than expected manufacturing growth, and despite concerns over the quality of new service sector employment, real GDP is now expected to have grown by just less than 1% during 1999.

The table below sets out the latest WERU forecasts for Wales for 2000 – 2002.

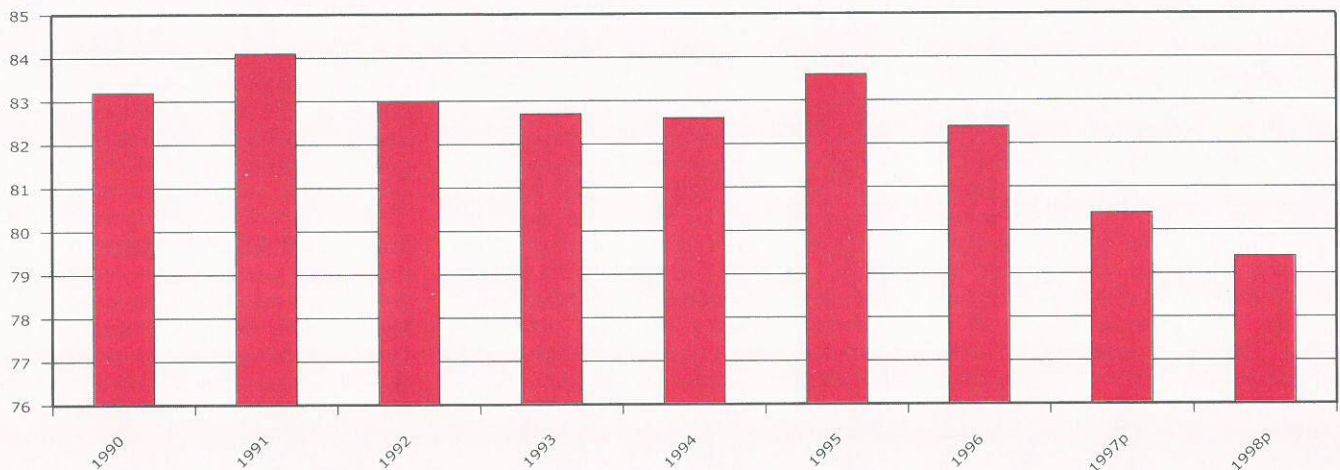
The forecast for 2000 and 2001 has been revised, slightly downwards to 1.8% and 2.0% respectively. These changes reflect an expectation that some parts of the service sector (e.g. finance and business services) will not now grow as fast as expected with, for example, recent expansions and new job announcements countered by losses as a result of rationalisation and closures. In addition parts of manufacturing, for example electronic engineering and steel, are expected to come under medium term pressure,

particularly as a result of the increasing competitive position of locations in the Euro-zone and Eastern Europe. Employment prospects in Welsh utilities also remain poor, with now almost the whole of the sector under external ownership following the take-over of Hyder by Western Power of the US.

Reference:

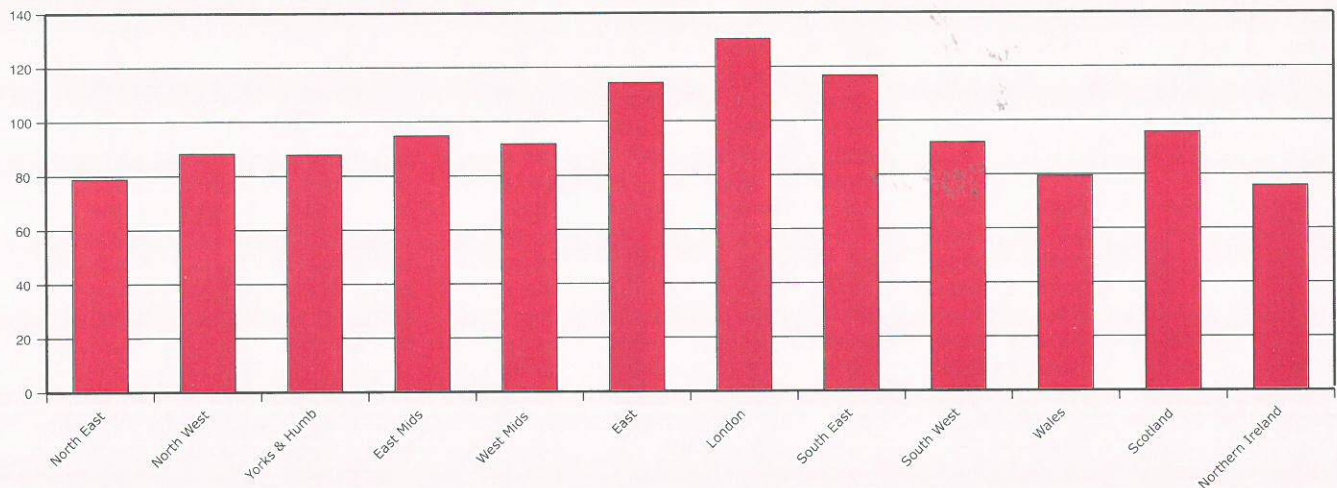
Huggins, R. (2000) *An Index of Competitiveness in the UK: Local, Regional and Global Analysis*, CASS, Cardiff University, April.

**Figure 2 Welsh GDP per head, 1990-1998, UK=100**



Source: ONS

**Figure 3 GDP per head by UK Region, 1998 (provisional), UK=100.**



Source: ONS

**Table 1 Forecast Change in Real GDP (%)**

	2000	2001	2002
Wales	1.8	2.0	2.1